

***United States Court of Appeals
for the Second Circuit***



**BRIEF FOR
APPELLANT**

74-1969-2341-2366

To be argued by
PETER K. LEISURE

United States Court of Appeals
FOR THE SECOND CIRCUIT

IIT, an International Investment Trust, and GEORGES BADEN,
JACQUES DELVAUX and ERNEST LECUIT, as Liquidators for IIT, an International Investment Trust,

Plaintiffs-Appellees-Cross-Appellants,

—against—

VENCAP, LTD., INTERVENT, INC., INTERCAPITAL, N.V.,
RICHARD C. PISTEIL, CHARLES E. MURPHY, JR.,
DAVID TAYLOR and HAVENS, WANDLESS, STITT &
TIGHE,

Defendants-Appellants-Cross-Appellees,

and

WALTER BLACKMAN,

and

ROBERT L. VESCO, MILTON F. MEISSNER,
NORMAN LeBLANC and STANLEY GRAZE,

Defendants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF DEFENDANTS-APPELLANTS-CROSS-APPELLEES
CHARLES E. MURPHY, JR., DAVID TAYLOR
and HAVENS, WANDLESS, STITT & TIGHE

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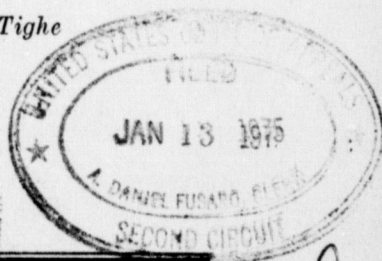


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United States Court of Appeals

FOR THE SECOND CIRCUIT

Docket Nos. 74-1969, 74-2341, 74-2366

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BADEN, JACQUES DELVAUX and ERNEST LECUIT, as Liquidators for IIT, an International Investment Trust,

Plaintiffs-Appellees-Cross-Appellants,

—against—

VENCAP, LTD., INTERVENT, INC., INTERCAPITAL, N.V., RICHARD
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HAVENS, WANDLESS, STITT & TIGHE,

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ON APPEAL FROM THE UNITED STATES DISTRICT COURT
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**BRIEF OF DEFENDANTS-APPELLANTS-CROSS-APPELLEES
CHARLES E. MURPHY, JR., DAVID TAYLOR
and HAVENS, WANDLESS, STITT & TIGHE**

Preliminary Statement

Defendants-appellants-cross-appellees Charles E. Murphy, Jr. ("Murphy"), David Taylor ("Taylor") and Havens,

Wandless, Stitt & Tighe ("Havens Wandless") appeal from an order of the United States District Court for the Southern District of New York, per the Honorable Charles E. Stewart, Jr., granting plaintiffs-appellees' motion for a preliminary injunction and for the appointment of a receiver. Judge Stewart's opinion and his subsequent order modifying that opinion are reproduced at pages 947a and 971a, respectively, of the joint appendix. Plaintiffs-appellees-cross-appellants brought this action for alleged violations of Section 10(b) of the Securities Exchange Act of 1934 [15 U.S.C. § 78j(b)] (the "Exchange Act") and Rule 10b-5 [17 C.F.R. § 240.10b-5] promulgated thereunder, as well as for alleged violations of Section 17(a) of the Securities Act of 1933 [15 U.S.C. § 77q(a)] (the "Securities Act"). In addition, plaintiffs-appellees have stated various pendent claims in the nature of common law fraud and corporate waste.

On June 10, 1974, the plaintiffs commenced this action and moved by Order to Show Cause for a preliminary injunction pursuant to Rule 65 of the Federal Rules of Civil Procedure and for the appointment of a receiver. On the same day the district court entered a temporary restraining order enjoining and restraining certain of the defendants from exercising any control over the present and future assets of IIT, Vencap Ltd. ("Vencap"), Intervent, Inc. ("Intervent") and Intercapital, N.V. ("Intercapital"). The temporary restraining order was modified on June 14, 1974, to eliminate the defendants Taylor, Murphy, and Havens Wandless.

At the conclusion of evidentiary hearings, the district court entered a preliminary injunction enjoining defendants Vencap, Intervent, Intercapital, and Richard C. Pistell ("Pistell"), and those under their control from exercising any control over the present and future assets of IIT, Vencap, Intervent and Intercapital. In addition, the district court appointed a receiver to take charge of all present

and future assets of IIT, Vencap, Intervent and Intercapital, in the possession and control of Pistell, Vencap, Intervent and Intercapital.

Murphy, Taylor and Havens Wandless bring this appeal pursuant to Title 28, United States Code, Sections 1292(a) (1) and 1292(a) (2), as aggrieved parties, in order to contest the district court's determination that it has jurisdiction over the subject matter of this action.

Statutes Involved

The following statutes and rules are involved in this appeal:

Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

...

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

S.E.C. Rule 10b-5 promulgated under the Exchange Act (17 C.F.R. § 240.10b-5) provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

Section 17(a) of the Securities Act [15 U.S.C. §77q(a)] provides:

It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) To employ any device, scheme, or artifice to defraud, or

(2) To obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) To engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 27 of the Exchange Act [15 U.S.C. §78aa] provides in relevant part:

The district courts of the United States, * * * shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all

suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this chapter or rules and regulations thereunder, or to enjoin any violation of such chapter or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. * * *

Section 22(a) of the Securities Act [15 U.S.C. §77v(a)] provides in relevant part:

The district courts of the United States, * * * shall have jurisdiction of offenses and violations under this subchapter and under the rules and regulations promulgated by the Commission in respect thereto, and, concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this subchapter. Any such suit or action may be brought in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the offer or sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. * * *

Title 28, United States Code, Section 1337 provides:

The district courts shall have original jurisdiction of any civil action or proceeding arising under any Act of Congress regulating commerce or protecting trade and commerce against restraints and monopolies.

Title 28, United States Code, Section 1332 provides in relevant part:

(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of \$10,000, exclusive of interest and costs, and is between—

(1) citizens of different States;

(2) citizens of a State, and foreign states or citizens or subjects thereof; and

(3) citizens of different States and in which foreign states or citizens or subjects thereof are additional parties.

...

(c) For the purposes of this section and section 1441 of this title, a corporation shall be deemed a citizen of any State by which it has been incorporated and of the State where it has its principal place of business . . .

(d) The word "States", as used in this section, includes the Territories, the District of Columbia, and the Commonwealth of Puerto Rico, . . .

Title 28, United States Code, Section 1350 provides:

The district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States.

Issues Presented For Review

1. Whether a United States Court has subject matter jurisdiction under the Securities Exchange Act of 1934 and the Securities Act of 1933 over an action arising out of a purchase, negotiated and closed outside of the United States, by a Luxembourg investment trust of shares in a Bahamian corporation, neither of whose shares are traded in the United States.

2. Whether, assuming that subject matter jurisdiction pursuant to the Securities Exchange Act of 1934 and the Securities Act of 1933 does not exist, the district court has jurisdiction over plaintiffs' non-Federal claims.

Statement of the Case

The Parties

Plaintiff, IIT, is an international investment trust organized under the laws of the Grand Duchy of Luxembourg, with an office and place of business in Luxembourg. It is an open-end mutual-fund, having no office or place of business in the United States. Plaintiff liquidators are citizens of Luxembourg, who represent that they have been authorized by the District Court of Luxembourg to collect IIT's assets and prosecute IIT's claims (A 9a, 196a, 286a-87a).*

* References in the form "A.....a" are to the joint appendix, which is comprised chiefly of the evidence submitted by plaintiffs during the hearings on the preliminary injunction application in the court below. In these hearings, plaintiffs not only presented live testimony, but submitted as exhibits transcripts of defendant Pistell's testimony in other proceedings, which included his examination by the SEC pursuant to subpoena in *Matter of International Controls Corporation* on November 1, 1972 (A 3877a-3958a); his testimony as a government witness during the preliminary injunction hearing in *S.E.C. v. Vesco* on April 12, 13, 16, 17 and 18, 1973 (A 1279a-1588a); and his post-hearing deposition in *S.E.C. v. Vesco* on May 6 and 7, 1974 (A 1660a-1868a).

Defendant Vencap, which was formed in June 1972, is a corporation organized and existing under the laws of the Commonwealth of the Bahama Islands with an office and principal place of business in Nassau, Bahamas. It has neither an office nor a place of business in the United States.* With the exception of qualifying shares, all of the ordinary shares of Vencap are owned equally by defendant Pistell, a United States citizen who is chairman of Vencap's Board of Directors as well as its President and Treasurer, and defendant Walter Blackman ("Blackman"),** a citizen and resident of the Bahamas who is a member of the Vencap Board of Directors and also serves as its Executive Vice President. All of the preference shares of Vencap are owned by IIT (A 9a-10a, 549a-50a, 552a-53a, 603a-05a, 676a, 702a-03a, 789a, 1189a-90a, 1197a-224a, 1228a-40a, 1688a-89a, 1691a, 1700a).

Defendant Intercapital, which was incorporated in December 1972, is a corporation organized and existing under the laws of the Netherlands Antilles with an office and principal place of business in the Bahamas. It has no office or place of business in the United States. Intercapital was formed as a not-for-profit financing vehicle to enable Ven-

* During Pistell's examination as a government witness in *S.E.C. v. Vesco*, he testified that, while in New York, there was an office set aside for him at the law offices of Havens Wandless at 99 Park Avenue (A 1662a-63a). Plaintiffs submitted the transcript of this testimony as an exhibit in the hearing below. See footnote, *supra* p. 7. From this cold record, the trial judge concluded that since Pistell testified that 99 Park Avenue was his office, it was therefore effectively the office of Vencap, Intervent and Intercapital (A 959a). In the hearing below, Pistell denied that Vencap had an office at the Havens Wandless office, and plaintiffs' counsel chose not to cross-examine him concerning any previous testimony on this subject (A 789a; see also A 538a, 671a-72a, 1670a).

** Blackman did not become either a shareholder or an officer of Vencap until May 21, 1973, more than seven months after the IIT investment in Vencap upon which this action is based (A 1252a-53a, 1268a). Blackman has not appeared in this action and it is not clear when, or whether, service of process was properly made upon him.

cap to make loans qualifying for favorable treatment under the tax treaty between the United States and the Netherlands, and is owned in equal shares by Pistell and Blackman (A 10a, 516a-20a, 555a, 672a, 1713a-16a).

Defendant Intervent, a wholly-owned subsidiary of Vencap, was incorporated in November 1973, more than a year after the formation of Vencap. It is a Delaware holding company which was formed to invest in oil and gas producing properties. Intervent has an office and principal place of business in the Bahamas. Although it has a registered office in Midland, Texas, it has no other office or place of business within the United States (A 10a, 521a-24a, 557a, 624a-26a, 672a, 1716a-17a, 2105a-07a).

Defendants Murphy and Taylor are members of the Bar of the State of New York, and partners in the defendant Havens Wandless, which is a New York City law firm with offices at 99 Park Avenue. Both were attorneys-in-fact for Pistell. Murphy initially was a director and Secretary of Vencap and Taylor an Assistant Secretary of Vencap. In addition, Taylor was the sole incorporator and Secretary of Intervent (A 568a-69a, 690a, 1186a, 1700a-02a, 2105a, 3990a-91a).*

All of the other defendants, namely, Robert L. Vesco ("Vesco"), Norman LeBlanc ("LeBlanc"), Milton F. Meissner ("Meissner"), and Stanley Graze ("Graze") were officers and directors in the corporate complex of IIT's

* With respect to the underlying transactions, Murphy, Taylor and Havens Wandless acted in their professional capacity as attorneys for Pistell and the corporate defendants (A 502a-03a, 513a-15a, 543a, 572a-73a, 580a-81a, 599a-600a, 675a, 685a-88a, 702a-03a, 750a, 1541a-42a, 1701a-02a, 1817a). Indeed, after reconsideration of all the evidence adduced on this subject, the trial judge modified his original opinion, which stated that "Pistell, Taylor, Murphy, Vencap, Intervent, Intercapital, and Havens, Wandless have engaged in Vencap's business activities. . ." to read: "Pistell, Taylor, Murphy, Vencap, Intervent, Intercapital and Havens, Wandless have engaged in activities. . ." (A 961a, 972a). (Emphasis added.)

"parent", IOS, Ltd., a foreign corporation doing business outside the United States. With the exception of LeBlanc, they are alleged by plaintiffs to be United States citizens, residing in foreign countries. LeBlanc, who was Executive Vice President of IOS, Ltd., is alleged by plaintiffs to be a Canadian citizen who resides in Costa Rica. Meissner was President of IIT Management Company, which acted as management company for IIT, as well as President of IOS, Ltd. Graze, a former professor of economics, was President of IOS Management Services, Limited (Bahamas) and International Capital Investments (Sterling) Ltd., London, England, which advised various IOS mutual funds; at one time he apparently acted as a consultant to and portfolio manager for Fund of Funds Limited ("FOF"), and Venture Fund (International) N.V. ("Venture Fund"), which were also in the IOS family, and/or IIT. No evidence with respect to the citizenship, residence or capacity in which these named defendants acted (other than with respect to Graze's capacity) was adduced in the court below. None of these defendants has appeared in this action and all are presently in default (A 10a-11a, 196a-97a, 199a-201a, 696a-97a, 1054a).*

The Complaint

The complaint alleges that defendants Pistell, Vesco, Meissner, Graze and LeBlanc conspired to defraud IIT and its shareholders of substantial sums of money for their personal benefit and use; that they caused the sale of all or most of IIT's readily marketable securities in United States securities markets**; that \$3,000,000 of the proceeds of these sales were invested in Vencap, a company formed

* Murphy, Taylor and Havens Wandless had no contact with Vesco, LeBlanc, Meissner and Graze in connection with the transactions which are the subject of this law suit (A 513a-15a, 672a-73a, 688a).

** IIT's securities and other assets in various European locations exceeded \$200,000,000 or \$300,000,000 at that period of time (A 460a-61a).

by defendant Pistell, in exchange for nonvoting preference stock and warrants of Vencap; that the investment in Vencap was a sham; that in connection with the investment, a three-page memorandum which contained material misstatements of fact and omitted to state material facts necessary to make the statements made not misleading, was delivered to IIT; and that the memorandum was not prepared for use in connection with the private placement of securities, but rather to provide cover in furtherance of the scheme.

The complaint contains twelve causes of action. The first and second causes of action claim that all defendants "singly and in concert" committed violations of Section 17(a) of the Securities Act and the second claims violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder. The ninth cause of action alleges that defendants Murphy, Taylor and Havens Wandless aided and abetted in the securities law violations and other claims. The remaining causes of action are pendent state claims alleging variously violation of Section 352-c of the General Business Law of the State of New York, conversion, common law fraud, corporate waste, breach of fiduciary obligations, failure to segregate IIT's funds and failure to disclose the alleged violations of law. Defendants Murphy, Taylor and Havens Wandless are specifically excepted from the third, fourth and fifth causes of action, but are included in the remaining causes of action in the complaint; and the eighth, ninth and eleventh pertain only to these defendants. In addition, the complaint seeks punitive damages in the sum of \$10,000,000.

The Facts

Some time in early 1972, Pistell met Graze in Nassau, Bahamas, in connection with a transaction unrelated to the present action. Over a period of weeks, in meetings conducted outside of the United States, they discussed the

philosophy of money markets, the perils of the stock market and particularly whether international monetary parity could be maintained. During one of Pistell's visits to London, England, Graze asked Pistell for his views regarding various investments which had been made in the past by FOF, IIT, and/or Venture Fund (collectively the "Funds"). Graze told Pistell that it was Graze's intention to advise the Funds to obtain a more liquid position in the event the Dow Jones average dropped below 1040. Pistell suggested that if he were in Graze's position, he would recommend investment in Japanese Yen, Deutschmarks and gold because he predicted (correctly as it turned out) that there would be further currency devaluations and a resulting increase in the world price for gold (A 696a-98a, 701a, 753a, 1305a-08a, 1821a-23a, 3889a, 3894a-95a).*

Thereafter, in early 1972, Pistell, who has extensive experience in locating and financing new ventures, decided to form a venture capital company in the Bahamas. Pistell met with various individuals in order to promote his concept; and one such individual with whom he discussed his plans was Graze (A 694a-96a, 708a, 1364a-66a, 1448a-57a, 1817a-18a).

In June 1972, Pistell contacted Murphy, who had represented Pistell in various legal matters for a number of years, to discuss his plans for the formation of the proposed venture capital company. Murphy, who maintains a residence in Nassau, Bahamas, and was there at the time, agreed to contact Carson, Lawson & Co. ("Carson Lawson"), a Bahamian law firm, regarding the incorporation of the proposed company (A 666a-67a). Carson Lawson formed Vencap on June 30, 1972, in accordance with Pistell's instructions. At the time of Vencap's incorporation, only ordinary shares of stock were authorized by Vencap's

* From April 1972 through October 1972, IIT had net sales of \$121,703,019 in United States securities (A 953a, 4046a-103a).

Memorandum of Association* ; and all of those shares were owned equally by Pistell and Count Amoury deRiencourt, a French citizen** (A 552a, 675a-76a, 1194a, 1236a, 1275a, 1367a).

Subsequent to the incorporation of Vencap, Pistell met with Graze in both the Bahamas and London, England, and in the course of those meetings told Graze that he and deRiencourt had established Vencap. At those same meetings, Graze indicated that one of the Funds he advised would be interested in investing in such a corporation. During August 1972, an agreement in principle was reached between Pistell and Graze whereby it was agreed that one of the Funds would invest \$3,000,000 in Vencap in the form of newly-authorized preference shares. Thereafter, Pistell caused a three-page memorandum to be prepared memorializing his discussions with IIT as to the formation of Vencap, its objectives and the initial transaction in which it was interested. The memorandum was prepared and typed in Nassau, Bahamas, and was delivered by hand to the attorneys for IIT in the Bahamas*** (A 75a-77a, 667a-68a, 674a-75a, 678a-80a, 698a-99a).

* The memorandum of association of a Bahamian company is equivalent to the articles of incorporation of an American company (A 1229a-39a).

** On May 21, 1973, Blackman became the owner of deRiencourt's shares (A 1252a, 1268a, 1548a-49a, 1637a).

*** In prior testimony in *S.E.C. v. Vesco*, Pistell testified that he requested Murphy or Taylor to prepare the three-page memorandum, that it was probably prepared by Murphy and that he thought it was mailed to Graze by his attorneys (A 1350a-51a, 1353a, 1814a-17a). In the hearing below, Murphy testified that he did not prepare the three-page memorandum and that it was not mailed to Graze by Havens Wandless (A 680a-85a). Taylor also testified that he had nothing to do with the preparation of the three-page memorandum and Pistell agreed that the memorandum was prepared in Nassau by Bahamian counsel, Carson Lawson (A 504a-05a, 699a-700a). The court below found only that the memorandum had been prepared at Pistell's instructions (A 953a-54a).

The specific terms and conditions of the Vencap preference shares, which were prepared jointly in Nassau, Bahamas, by Bahamian counsel and Willkie, Farr & Gallagher ("Willkie Farr"), a New York City law firm representing IIT, were adopted by the Vencap Board in Nassau on August 29, 1972 (A 504a-05a, 531a-32a, 599a-600a, 667a-68a). On August 31, 1972, at an extraordinary general meeting, the Vencap shareholders authorized the issuance of 30,000 preference shares (A 1602a-04a).

During September 1972, Willkie Farr prepared an agreement setting forth the terms of IIT's investment in Vencap and presented it to Carson Lawson and Havens Wandless for review (A 501a, 504a-05a, 600a, 661a-62a, 685-89a, 1605a-06a, 3965a-76a, 4155a). The agreement provides that the preference shares have no vote, are entitled to a six percent noncumulative dividend (which has priority over dividends to ordinary shareholders) when and as declared, are to share in one-third of the net earnings of Vencap when and as declared, and are redeemable at par plus six percent for the portion of the year of redemption (A 1607a-09a).*

The agreement between IIT and Vencap was signed on September 29, 1972, in Nassau, Bahamas, by Meissner on behalf of IIT and by Pistell on behalf of Vencap (A 505a-09a, 531a-32a, 1C05a-06a). On October 6, 1972, the attorneys for Vencap and IIT met in Nassau for the closing, as pro-

* Contrary to plaintiffs' contentions in the court below, the terms and conditions of the preference stock and the agreement between IIT and Vencap were not negotiated by Havens Wandless or any of its partners; and the only United States contact in this regard was an exchange of drafts of the IIT/Vencap agreement between Havens Wandless and Willkie Farr in New York (A 501a-06a, 513a-14a, 543a, 599a-603a, 685a-88a, 1605a-11a, 1826a-27a, 3965a-76a, 4155a). Indeed, at the insistence of IIT's attorneys, Willkie Farr, who informed Taylor that IIT was precluded from engaging in business activities in the United States by a 1967 SEC consent decree, all material aspects of the transactions leading up to the IIT investment in Vencap were conducted outside the United States (A 504a-05a).

vided by the September 29 agreement, but were advised that the IIT funds necessary for the closing had not yet been received by the Bahamas Commonwealth Bank ("BCB"). The closing eventually took place on October 9, 1972, in the Bahamas. Although neither Vencap, Pistell nor Vencap's counsel knew the source of the IIT funds used to purchase the Vencap preference shares, the funds apparently came directly from cash balances maintained by IIT in Luxembourg by Overseas Development Bank Luxembourg, the cash custodian for IIT* (A 450a, 459a, 461a-62a, 467a-72a, 476a-77a, 509a-12a, 1632a, 4108a, 4237a).

Within a few days after the closing, the \$3,000,000 Vencap received from IIT for the preference shares was transferred by Vencap from BCB to the Chase Manhattan Bank in London ("Chase"). The funds were transferred to Chase because Chase offered a Eurodollar interest rate which was higher than the rate offered by BCB (A 528a-29a).

The Alleged Non-Disclosures and Misrepresentations

Plaintiffs' non-disclosure allegations are based upon alleged material omissions from the three-page memorandum. Thus, plaintiffs contend that the three-page memorandum failed to disclose the nature of the preference shareholders' rights in Vencap's profits (although a copy of the Vencap resolution which set forth the extent of those rights was annexed to the three-page memorandum and the September 29, 1972 agreement signed by IIT (A 466a-69a)); the extent of Pistell's compensation and reimbursable expenses; that Vencap planned to invest in Out Islands Airways (a Bahamian carrier); that Pistell would make loans from and

* Plaintiffs contend, and the district court found, that the \$3,000,000 used to purchase the Vencap preference shares, came from the sale of IIT's United States securities by American National Bank & Trust Company ("ANBT") of Montclair and Morristown, New Jersey, which held those securities as sub-custodian for Montreal Trust Company, Montreal, Canada, a securities custodian for IIT (A 417a, 457a, 473a-74a).

through Vencap and Intercapital; that Vencap would invest in United States securities; and that Pistell was subject to Federal tax liens, was in default on a bank loan and was in arrears in alimony payments.

Plaintiffs also assert that the three-page memorandum contained material misrepresentations with respect to the purpose for which Vencap was organized; the nature of Vencap's management; the persons to whom Vencap shares would be offered; and a proposed Vencap investment in a leading Caribbean air carrier, as well as other proposed Vencap investments.

While defendants contend that each of the alleged omissions and misrepresentations was either disclosed to IIT prior to the time it invested in Vencap or was not material, those issues are not squarely before the Court. The issue here is the presence or absence of subject matter jurisdiction; and, as this brief will show, the alleged omissions and misrepresentations do not provide sufficient contact with the United States to sustain a finding of such jurisdiction.

The Challenged Transactions

In addition to the alleged non-disclosures upon which they base their securities law claims, plaintiffs also contend that certain Vencap transactions, unrelated to the IIT investment in Vencap in both time and circumstance, were improper. These "challenged transactions", which include loans to Pistell from Intercapital and Intervent, Pistell's use of a finder's fee which was earned in a transaction unrelated to Vencap, salary payments to Blackman and Pistell, and certain Vencap investments in Canadian and Bahamian corporations, form the basis for plaintiffs' state law claims.

Whatever relevance these transactions, which defendants maintain were completely proper, might have to the

question of whether a preliminary injunction should have been granted, they are totally irrelevant to the basic issue of whether subject matter jurisdiction under the securities laws exists. As the challenged transactions took place long after IIT invested in Vencap, they are completely unrelated to plaintiffs' securities law claims, which, of course, concern only IIT's inducement to purchase the Vencap preference shares. In short, the challenged transactions do not provide a basis for the securities law claims involved herein, and therefore cannot provide a basis for jurisdiction over such claims. This fact was clearly recognized by the district court, which did not rely upon any of the challenged transactions in finding that subject matter jurisdiction over this action existed.

The Decision of the District Court

In determining that it had subject matter jurisdiction, the court found that several of the defendants had various contacts with the United States (which the district court did not connect to the transaction in question); that approximately 300 United States citizens and residents are fundholders in IIT*; that IIT used a portion of the proceeds from the sale of its United States securities, which were held at ANBT in New Jersey, to purchase the Vencap preference shares and that those funds were transferred from ANBT to the Bahamas, designated for Vencap.** The court further found that ANBT received and kept the certificates and warrant for the Vencap preference shares in New Jersey, and that a substantial portion of the \$3,000,000 received by Vencap was thereafter invested in United States securities.

* This finding was based solely on inadmissible evidence which was not even before the district court at the time it rendered its decision. See discussion, *infra* at pp. 26-28.

** There is no basis in the record for this finding. See p. 29. Moreover, there was no finding that the sale of IIT securities was induced by any of the defendants.

After setting forth these findings, the court held that subject matter jurisdiction pursuant to the Federal securities laws was present because defendants,

Pistell, Taylor, Murphy, Vencap, Intervent, Intercapital and Havens, Wandless have engaged in activities, a significant portion of which occurred in the United States or which have had a substantial and foreseeable impact on United States investors. (A 972a)

The court also found that it had subject matter jurisdiction pursuant to 28 U.S.C. Section 1337 (a civil action arising under an Act of Congress regulating commerce or protecting trade and commerce against restraints and monopolies) and that it had *probable* subject matter jurisdiction over plaintiffs' non-securities law claims pursuant to 28 U.S.C. Section 1332 (diversity of citizenship with an amount in controversy exceeding the sum of \$10,000, exclusive of interest and costs), 28 U.S.C. Section 1350 (an action by an alien for a tort committed in violation of the law of nations or a treaty of the United States) and Section 302 of the New York Civil Practice Law and Rules, as well as under the doctrine of pendent jurisdiction.

POINT I

The Court Lacks Subject Matter Jurisdiction Over Plaintiffs' Federal Securities Law Claims.

It is clear that the provisions of the Federal securities laws may, under certain circumstances, be applicable to transactions in the securities of foreign issuers. *Leasco Data Processing Equipment Corporation v. Maxwell*, 468 F. 2d 1326 (2d Cir. 1972). However, it is equally clear that those laws cannot reach all such transactions, as domestic law may be applied only to conduct which has a significant nexus with the United States.* *Leasco Data Processing Equipment Corporation v. Maxwell*, *supra*; *Schoenbaum v. Firstbrook*, 405 F. 2d 200 (2d Cir. 1968), *rev'd in part on other grounds*, 405 F. 2d 215 (2d Cir. 1968) (en banc), *cert. denied sub. nom. Manley v. Schoenbaum*, 395 U.S. 906 (1969).

In *Leasco Data Processing Equipment Corporation v. Maxwell*, *supra*, this Court held that substantial fraudulent misrepresentations made to American investors in the United States, plus other United States contacts, constitute a sufficient predicate for the exercise of subject matter jurisdiction over a transaction involving the purchase of foreign securities abroad. Earlier, in *Schoenbaum v. First-*

* Subject matter jurisdiction over plaintiffs' Federal securities law claims, if it exists, must be based upon Section 27 of the Exchange Act and Section 22(a) of the Securities Act, which grant jurisdiction over violations of those Acts to the district courts of the United States. For purposes of the extraterritorial reach of the Federal securities laws these sections are co-extensive. This conclusion is dictated by the similarities in language and purpose of the two sections. See *United States v. Clark*, 359 F. Supp. 131, 133 (S.D.N.Y. 1973); cf. *Leasco Data Processing Equipment Corporation v. Maxwell*, *supra*. Indeed, the elements of a private action under Section 10(b) of the Exchange Act and Section 17(a) of the Securities Act, the two sections under which plaintiffs bring their securities law claims, are the same. *Lanza v. Drexel & Co.*, 479 F. 2d 1277, 1280 n.2 (2d Cir. 1973) (en banc).

brook, supra, this Court found jurisdiction over an action involving fraudulent acts committed outside the United States in connection with a transaction in foreign securities, because the transaction in question was detrimental to the interests of American investors and involved foreign securities registered and listed on an American securities exchange. In so holding, the *Schoenbaum* Court stated:

We believe that Congress intended the Exchange Act to have extraterritorial application in order to protect domestic investors who have purchased foreign securities on American exchanges and to protect the domestic securities market from the effects of improper foreign transactions in American securities. 405 F.2d at 206.

As the facts herein do not come within either the *Schoenbaum* or *Leasco* holdings, which, together, constitute the law in this Circuit regarding the extraterritorial application of the antifraud provisions of the Federal securities laws, jurisdiction over the instant action is clearly lacking. The case at bar is surely wide of the *Schoenbaum* rule, as this action involves a purchase by a foreign entity of foreign securities—IIT's purchase of Vencap's preference shares—which are neither registered on an American securities exchange nor traded in the United States. Neither does this action fall within the *Leasco* holding because if misrepresentations or omissions inducing plaintiffs to purchase the Vencap shares were made at all, such misrepresentations or omissions must have been made in the Bahamas, where the IIT/Vencap transaction was negotiated and consummated. Moreover, irrespective of the question of where the alleged fraud took place, the *Leasco* rule requires that the defrauded purchaser be an American; and here the plaintiff investor is clearly foreign.

Contrary to the implication contained in the district court's opinion, the record clearly indicates that all of the documents relating to IIT's investment in Vencap

were in fact prepared outside the United States. The three-page memorandum, which plaintiffs contend, and the district court found, partially induced IIT to purchase the Vencap shares, was prepared and delivered in the Bahamas* (A 75a-77a, 504a, 674a-75a, 678a-80a, 684a-85a, 954a, 961a). The September 29, 1972 agreement, which set out the terms and conditions of the IIT purchase, was also prepared, executed and delivered to plaintiff IIT *only in the Bahamas* (A 501a, 504a-05a, 507a, 531a-32a, 599a-600a, 661a-62a, 685a-89a); and the mere exchange of drafts of that agreement in New York by Vencap's and IIT's lawyers is an insufficient United States contact upon which to base jurisdiction.** *See Investment Properties International, Ltd. v. I.O.S., Ltd.*, [1970-71 Transfer Binder] CCH Fed. Sec. L. Rep. ¶93,011 (S.D.N.Y. 1971), *aff'd without opinion* (unreported 2d Cir. 1971).***

Thus, clearly unable to ground its jurisdictional holding upon either fraudulent activity in the United States or a transaction in securities traded on American securities markets, the district court instead based its determination on the following facts which it found jurisdictionally relevant: (a) various United States contacts unrelated in time and substance to the allegedly improper transactions, (b) the existence of United States shareholders of

* The court below made no finding as to where the memorandum was prepared. See footnote, p. 13 *supra*.

** Although the district court found that a significant portion of the legal work performed by defendants Taylor and Havens Wandless was done in the Southern District of New York, the record is clear that none of this work was in connection with the transaction upon which plaintiffs base their securities law claims. As already indicated at page 14, the exchange of drafts of the IIT/Vencap agreement between Havens Wandless and Willkie Farr in New York City was the *only* United States contact with the allegedly wrongful activity.

*** This Court's unreported affirmance without opinion is noted in *Investment Properties International, Ltd. v. I.O.S., Ltd.*, 459 F. 2d 705, 706 n. 1 (2d Cir. 1972).

IIT, and (c) the transfer of certain funds used for IIT's purchase of the Vencap preference shares from ANBT in New Jersey to BCB in the Bahamas. Each of these "facts" is patently insufficient to support a finding of subject matter jurisdiction under either the *Schoenbaum* or *Leasco* rules and, moreover, those denominated "(b)" and "(c)" are also completely unsupported by the record.

In determining the parties' United States contacts, the district court found that defendants Havens Wandless, Taylor, Murphy, Pistell, Vencap, Intervent and Intercapital transact business in New York, New York; that various transactions and pieces of mail for Vencap and to a lesser extent for Intervent and Intercapital were initiated, directed and consummated from and received at 99 Park Avenue, New York, New York; that 99 Park Avenue was Pistell's office and therefore effectively the office of Vencap, Intervent and Intercapital; that Vencap's financial records are maintained in the office of its accountants in Great Neck, Long Island; that transactional records of Vencap were maintained at 99 Park Avenue; that on November 16, 1973, Pistell signed an Application Form for a Certificate of Authority to do business in the State of Louisiana stating that his address was 99 Park Avenue; that Pistell conducted the business of Vencap in the Southern District of New York during the period relevant to this action; and that a substantial portion of the \$3,000,000 received by Vencap was thereafter invested in United States securities* (A 959a-60a).

Significantly, in reviewing the defendants' United States contacts, the district court failed to connect those contacts, in either time or substance, to the alleged fraud. The court's failure to engage in such an analysis underscores the lack of relevance the district court's list of American

* There is not even an allegation that Vencap's portfolio investment in United States securities was in any way improper, actionable or violative of the securities laws

contacts has to the issue of subject matter jurisdiction. Had such a review been made, it would have become overwhelmingly apparent that the so-called American contacts were completely unrelated to the IIT purchase of the Vencap preference shares. Without such relationship they are irrelevant to plaintiffs' securities law claims and therefore equally irrelevant to the issue of subject matter jurisdiction.

The record is clear that the meetings which led up to IIT's purchase of the Vencap shares were not held in the United States nor were the documents relating to that transaction prepared in this country (A 501a, 504a-09a, 531a-32a, 599a-600a, 661a-62a, 667a-68a, 674a-75a, 678a-80a, 684a-89a, 698a-99a). It therefore follows that any business Havens Wandless, Taylor, Murphy, Pistell, Vencap, Intervent or Intercapital transacted in New York (including receiving or sending mail), was completely unrelated to IIT's investment in Vencap. Indeed, the record shows that the mail apparently referred to by the court below relates to a time period long after IIT purchased the Vencap preference shares.*

The record is devoid of a single shred of evidence, or even a bare allegation, that the storing of Vencap's financial records at an accountant's office on Long Island or the similar maintenance of other Vencap records at 99 Park Avenue induced, or was even contemporaneous with, IIT's investment in Vencap. Nor could either Pistell's application for a Certificate of Authority to do business in Louisiana or Vencap's investment in securities have any bearing on the IIT/Vencap transaction, as both took place well after that transaction was consummated.

Since mere contacts with the United States, which are unrelated to the transactions upon which the action is

* Examples of such mail appear in plaintiffs' exhibit 14-41 which commences at p. 2183a of the joint appendix.

based, are insufficient to sustain subject matter jurisdiction under the Federal securities laws, the aforementioned contacts cannot provide a basis for finding subject matter jurisdiction over this action. *Finch v. Marathon Securities Corporation*, 316 F. Supp. 1345 (S.D.N.Y. 1970). Were this not the rule, a potential plaintiff could tie *any United States contact* a foreign corporation might have to *any foreign purchase* of that corporation's securities and, by some legal alchemy, convert the mere existence of those facts into a securities law claim with a full-blown jurisdictional base. Such a result surely defies both logic and international law. While presence and activity within the Southern District of New York may establish a basis for personal jurisdiction, it is in no way relevant to the issue of subject matter jurisdiction.*

To sustain subject matter jurisdiction, the defendants' conduct within the United States must not only be "significant", it must also constitute an "essential link" in the alleged fraud. Thus, there must be a causal connection between the United States conduct and the damage alleged by plaintiffs. *Leasco Data Processing Equipment Corp. v. Maxwell*, *supra*. Incidental acts, or incidental use of an instrumentality of interstate commerce, which are not part of the essence of the alleged violation, simply cannot provide a basis for jurisdiction. In short, plaintiffs must show at a minimum that the defendants engaged in fraudulent acts within the United States which "significantly whetted" IIT's interest in acquiring Vencap securities. *Leasco Data Processing Equipment Corp. v. Maxwell*, *supra* at 1335.

* The fact that the district court confused the standards relevant to personal jurisdiction with the standards relevant to subject matter jurisdiction is highlighted by the district court's finding that it had probable subject matter jurisdiction pursuant to Section 302 of New York Civil Practice Law and Rules (A 960a-61a). Of course, no authority beyond CPLR 302 itself is required to sustain the fundamental proposition that it relates only to personal jurisdiction.

Since such a showing cannot be based upon the district court's general list of United States contacts, all of which are unrelated to the alleged fraud, that list is meaningless for purposes of subject matter jurisdiction.

The district court itself clearly did not find the foregoing United States contacts sufficient for jurisdictional purposes and relied heavily upon its determination that approximately 300 United States citizens and residents are fundholders of IIT. Indeed, during the course of the proceedings below, the district court indicated that a showing of United States fundholders would satisfy it that subject matter jurisdiction was present (A 926a). However, the mere American citizenship of the purchaser or seller in a foreign securities transaction is an insufficient basis upon which to predicate subject matter jurisdiction under the Federal securities laws. *Garner v. Pearson*, 374 F. Supp. 591, 598 (M.D. Fla. 1974).

On the instant facts, the *Garner* rule is even more compelling because the Americans in question are not themselves the purchasers of the Vencap securities, but rather are fundholders in a foreign investment trust which was the actual purchaser. Reliance upon the existence of such fundholders as a basis for determining subject matter jurisdiction would lead to a result which is beyond reason, Congressional intent and the bounds of international law. If the presence of United States shareholders in a plaintiff or defendant foreign corporation were in itself a sufficient predicate for subject matter jurisdiction, the United States would find itself subjecting substantially all foreign transactions in the shares of major *publicly traded* foreign corporations to the scrutiny of the Federal securities laws.*

* If the United States were to adopt such a rule, foreign nations might seek to impose their regulations upon United States citizens and corporations involved in corresponding transactions that are essentially American. See *Lauritzen v. Larsen*, 345 U.S. 571, 582 (1953).

The *Leasco* Court implicitly recognized this by concluding that a publicly held United States corporation's purchase of foreign securities not traded in the United States, which was fraudulently induced in a foreign country, would not result in the type of effect within the United States required to confer jurisdiction on the Court even though the securities of the defrauded American corporation are traded on the New York Stock Exchange. *Leasco Data Processing Equipment Corp. v. Maxwell*, *supra* at 1334. Thus *a fortiori*, where, as here, the alleged United States contact is the mere presence of American fundholders in a *foreign entity* (not listed or traded in the United States) which claims to have been fraudulently induced to purchase foreign securities abroad, the United States nexus is too slight to confer jurisdiction.*

Even if the existence of 300 United States shareholders were determinative of the issue of subject matter jurisdiction, such jurisdiction would not be present because there was no competent evidence that IIT had American shareholders before the district court. The district court's determination that such shareholders existed was apparently made solely on the basis of the affidavit of Peter G. Wood, who claims to have been responsible for the maintenance

* Although the Court found subject matter jurisdiction present in *S.E.C. v. United Financial Group, Inc.*, 474 F. 2d 354 (9th Cir. 1973), where only three American investors were ascertained, the facts in that case are readily distinguishable from those in the case at bar. In contrast with the facts at hand, in *United Financial Group* the defendants had engaged in direct sales activities with United States citizens and there were very substantial improper activities in the United States. Additionally, here, the purchaser-plaintiff is a foreign entity and if any Americans are involved at all, they are merely several of its many shareholders who are predominantly foreign; in *United Financial Group* the direct investors were individual American nationals. Moreover, it is stated in IIT's prospectus dated March 31, 1970, that its shares were neither offered for sale nor sold to United States citizens or United States residents (A 1021a).

of the records of IIT's fundholders since 1966 (A 154a-55a). The Wood affidavit, which was sworn to on July 23, 1974, *twenty days after* the date of the district court's decision, was submitted as a result of the court's ruling that plaintiffs' oral and documentary evidence failed to prove that IIT had any United States shareholders. Among the reasons for that failure of proof, which were revealed on cross-examination, was the fact that plaintiffs' witness not only lacked personal knowledge of whether IIT had United States shareholders, but also lacked personal knowledge of the factual basis and method of preparation of the documentary evidence which, according to plaintiffs, indicates the existence of such shareholders. Additionally, that documentary evidence, which purports to contain a list of American shareholders of IIT, apparently reflects IIT shareholders as of 1973, and therefore does not indicate the existence of any such shareholders at the time IIT purchased the Vencap preference shares (A 230a-34a). Plaintiffs attempted to circumvent this gap in their own evidence by a letter to the district court, dated July 2, 1974, in which plaintiffs' counsel stated that IIT had United States shareholders and that an affidavit to that effect would be forthcoming (A 151a-53a).*

It is beyond dispute that prior to rendering a decision, a court must have before it admissible evidence of the facts upon which the decision is based. Anything less would surely be a denial of the essential fairness we call due process. As the district court based its determination of subject matter jurisdiction predominantly upon the presence of American shareholders of IIT—a fact which was not even colorably in evidence when the court rendered its decision—that determination must be reversed.

In addition, the district court's reliance upon such post-hearing "evidence" obviously denied defendants the essen-

* The letter was hand delivered to the district court the day before its decision was rendered, and 11 days after a full evidentiary hearing had been completed.

tial right of cross-examination. Cross-examination of Wood, not to mention plaintiffs' counsel, whose letter was the sole evidence of the existence of United States shareholders before the court at the time it rendered its decision, might well have led to a determination identical to that which resulted from defendants' cross-examination of the original witness through whom plaintiffs sought to show the existence of United States shareholders.

Moreover, even assuming *arguendo* that the Wood affidavit was timely, the law in this Circuit is clear: an order on a preliminary injunction may not issue on the basis of affidavits where a hearing is possible and there are disputed issues of fact. *Carter-Wallace, Inc. v. Davis-Edwards Pharmacal Corp.*, 443 F.2d 867 (2d Cir. 1971); *Cerruti, Inc. v. McCrory Corp.*, 438 F.2d 281 (2d Cir. 1971). Here the possibility of a hearing is manifest as such a proceeding took place over seven court days and generated 774 pages of testimony. Thus, the district court's finding that approximately 300 United States citizens and residents are IIT fundholders is a nullity; and no determination of subject matter jurisdiction, or of anything else, may rest upon it.*

The Court below also found jurisdictionally significant its determination that IIT's United States securities were held at ANBT in New Jersey; that ANBT received instructions to transfer \$3,000,000 of the proceeds from the sale of those securities to the BCB account at ANBT in New Jersey; and that ANBT then caused the \$3,000,000 to be transferred from the BCB account at ANBT to BCB in

* The Wood affidavit states that as of December 31, 1972, long after the Vencap transaction had been entered into, IIT had as shareholders 111 United States citizens residing abroad, 67 United States citizens residing in the United States, and 159 non-citizen United States residents. Even if the Wood affidavit is accepted as true, and in evidence, there is still nothing in the record to indicate that IIT had United States shareholders at the time the IIT/Vencap transaction was entered into.

the Bahamas designated for Vencap.* While these contacts with a New Jersey bank may at first glance seem to provide a superficial United States gloss to a clearly foreign transaction, they cannot support the district court's exercise of jurisdiction over this action.

Where IIT originally kept its United States securities, and whether \$3,000,000 of the proceeds from the sale of those securities was transferred to the BCB account at ANBT are both totally irrelevant to the question of subject matter jurisdiction. There has been no finding that the sale of IIT's securities was in any way connected with the IIT/Vencap transaction; and as already demonstrated, without such a connection those facts are meaningless, under the *Leasco* rule, for jurisdictional purposes.

The district court's finding that the \$3,000,000 IIT used to purchase the Vencap preference shares was part of the proceeds of IIT's sale of its United States securities is not only jurisdictionally irrelevant but also unsupported by the record. The only witness plaintiffs called in support of that theory, a vice president and trust officer of ANBT, testified that he had no knowledge that the IIT funds transferred to BCB for the Vencap transaction arose from the sale of IIT's United States securities (A 467a-68a). Indeed, a review of the record indicates that the IIT funds used for the Vencap transaction apparently came directly from cash balances maintained in Luxembourg (A 450a, 459a, 461a-62a, 467a-72a, 476a-77a, 509a-12a, 4108a, 4237a).

However, even if the funds had come from the proceeds of the sale of IIT's United States securities, that fact

* In addition, the district court found that ANBT received and kept the certificates and warrant for the Vencap preference shares in New Jersey. Of course, this fact has no jurisdictional significance because it relates to the time period subsequent to the IIT/Vencap transaction. Clearly plaintiffs' securities law claims are, and must be, based upon an alleged improper inducement to purchase the Vencap shares, and not on later events.

could not sustain jurisdiction because the record contains no indication that the defendants induced IIT to use *those* funds to purchase the Vencap preference shares; nor is there any indication at all of improper activity in the United States in connection with the alleged transfer of the \$3,000,000 to the Bahamas. Thus, the district court's "proceeds theory" will not support jurisdiction under the *Leasco* principle; and the mere removal from the United States of a portion of the proceeds of a legitimate securities transaction can hardly result in the adverse impact on American investors or the American securities market required to sustain jurisdiction under the *Schoenbaum* test. Moreover, the defendants surely could not have foreseen that IIT, headquartered in Europe, would use funds it held in the United States to purchase the Vencap shares. Thus, under any accepted test, the alleged transfer of a portion of the proceeds of the sale of IIT's United States securities cannot sustain subject matter jurisdiction.

Since this Court spoke in *Leasco* and *Schoenbaum*, other courts have interpreted these two watershed cases broadly. The *Leasco* holding has been extended by determining that "significant conduct within the territory" which is essentially linked to the alleged fraud is a sufficient basis for subject matter jurisdiction (even though the allegedly fraudulent acts took place outside the United States), *Bersch v. Drexel Firestone, Inc.*, CCH Fed. Sec. L. Rep. ¶94,889 (S.D.N.Y. 1974); and the *Schoenbaum* holding has been extended by finding "jurisdictional" impact upon American investors even where the securities involved are not traded in United States securities markets, see *S.E.C. v. United Financial Group, Inc.*, *supra*. Although the cases promulgating such far-reaching holdings may claim to be the progeny of *Leasco* and *Schoenbaum*, they clearly fail to heed their precursors' admonitions. For in *Leasco*, this Court stated:

When no fraud has been practiced in this country and the purchase or sale has not been made here, we would be hard pressed to find justification for going beyond *Schoenbaum*, 468 F.2d at 1334.

However, even assuming that *Leasco* and *Schoenbaum* do not chart the farthest reaches of the extraterritorial application of the American securities laws, it has been amply demonstrated that the United States contacts and effects in the instant action are too thin, under any theory, to support the jurisdiction which plaintiffs assert.

In sum, jurisdiction over this action pursuant to the Federal securities laws is lacking because no material misrepresentations or omissions were made in the United States, plaintiffs' and defendants' various United States contacts were completely unrelated to the allegedly fraudulently induced transaction in both time and circumstance, and there has been no showing that the transactions complained of have had a substantial impact upon American investors or the American securities markets.

POINT II

The Non-Securities Law Bases Upon Which Plaintiffs Assert Subject Matter Jurisdiction Are Also Insufficient to Confer Jurisdiction Over This Action.

In addition to finding subject matter jurisdiction over this action pursuant to Section 27 of the Exchange Act and Section 22(a) of the Securities Act, the district court found that it had jurisdiction under Section 1337 of the Judicial Code, 28 U.S.C. § 1337. The court below also noted that it had *probable* jurisdiction pursuant to: Section 1332 of the Judicial Code, 28 U.S.C. § 1332; Section 1350 of the Judicial Code, 28 U.S.C. § 1350; Section 302 of the New York Civil Practice Law and Rules (the "CPLR"); and the doctrine of pendent jurisdiction. Despite the district

court's bald conclusion to the contrary, an analysis of the applicable cases and statutes clearly indicates that subject matter jurisdiction over this action may not be predicated upon any of the aforementioned bases.

Section 1337 of the Judicial Code

Section 1337 of the Judicial Code provides that the district courts of the United States shall have original jurisdiction over civil actions or proceedings arising under an Act of Congress regulating commerce or protecting trade and commerce against restraints and monopolies. Section 1337 does not itself create a cause of action, *Colorado Labor Council, AFL-CIO v. American Federation of Labor & Congress of Industrial Organizations*, 481 F.2d 396, 400 (10th Cir. 1973), but rather provides a statutory basis for the exercise of jurisdiction over actions concerning the validity, construction or enforcement of statutes regulating interstate or foreign commerce. *Adams v. International Brotherhood of Boilermakers, Iron Ship Builders, Blacksmiths, Forgers & Helpers*, 262 F.2d 835, 839 (10th Cir. 1959).

Although there appears to be no case law governing the application of Section 1337 to Federal securities law claims, this dearth of authority is readily explained. Section 1337 is a general jurisdiction statute, presumably enacted by Congress to permit recourse to the Federal courts when rights assured by Federal statutes which do not contain direct grants of subject matter jurisdiction are violated. Since both the Exchange Act and the Securities Act—the only Acts of Congress upon which plaintiffs base the instant action—contain jurisdictional provisions, Section 1337 is irrelevant to a determination of whether jurisdiction over claims brought under those statutes exists.

It has already been demonstrated that neither Section 27 of the Exchange Act nor Section 22(a) of the Securities

Act provides a basis for the exercise of subject matter jurisdiction over this action. *A fortiori*, if there is no jurisdiction pursuant to the securities laws, there can be no jurisdiction under Section 1337:

It is clear that general statutes [referring to Section 1337] do not confer jurisdiction where an applicable regulatory statute precludes it. *United Electrical Contractors Association v. Ordman*, 258 F. Supp. 758, 762-763 (S.D.N.Y. 1965), *aff'd*, 366 F.2d 776 (2d Cir. 1966), *cert. denied*, 385 U.S. 1026 (1967).

In short, if the securities laws themselves will not sustain subject matter jurisdiction over this action, it would be anomalous to find such jurisdiction on the basis of Section 1337.

Section 1332 of the Judicial Code

Section 1332 of the Judicial Code provides that the district courts shall have original jurisdiction over civil actions in which the amount in controversy exceeds \$10,000 and the action is between: (1) citizens of different states; (2) citizens of a state and foreign states or foreign nationals; or (3) citizens of different states and in which foreign states or foreign nationals are additional parties.

The instant action clearly does not fall within Section 1332 because "complete diversity" between plaintiffs and defendants is lacking. The plaintiffs herein are a Luxembourg investment trust and its Luxembourg liquidators, while the defendants are a Bahamian corporation (Ven-cap), a Netherlands Antilles corporation (Intercapital), a United States corporation (Intervent), a Bahamian citizen (Blackman), a Canadian citizen (LeBlanc), American citizens (Pistell, Taylor, Murphy, Vesco, Meissner and Graze), and an American law firm (Havens Wandless). The Federal courts have no diversity jurisdiction over

an action in which the plaintiffs and any of the defendants are aliens. *Leasco Data Processing Equipment Corp. v. Maxwell*, *supra* at 1333; *Finch v. Marathon Securities Corp.*, *supra* at 1349.

It is well settled that in order to sustain jurisdiction of an action based on diversity of citizenship in the federal court, each plaintiff must be capable of suing each defendant in that court . . . The courts of the United States have no jurisdiction of a case in which both parties are aliens, . . . ; if both a party plaintiff and a party defendant are aliens the district court lacks jurisdiction, even though there are other parties in the action, as plaintiffs or defendants, who are citizens of the United States. *Tsitsinakis v. Simpson, Spence & Young*, 90 F. Supp. 578, 579 (S.D.N.Y. 1950).

Section 1350 of the Judicial Code

Section 1350 of the Judicial Code provides the Federal district courts with jurisdiction over actions brought by aliens for torts committed in violation of the law of nations or a treaty of the United States. It is irrelevant to the case at bar because plaintiffs' claims, based upon the antifraud provisions of the Federal securities laws, the New York General Business Law, conversion, common law fraud, corporate waste, breach of fiduciary duty and failure to segregate funds, simply do not allege either a violation of the law of nations or of a treaty of the United States.

A violation of the law of nations arises only when there is

. . . a violation by one or more individuals of those standards, rules or customs (a) affecting the relationship between states or between an individual and a foreign state, and (b) used by those states for their

common good and/or in dealings *inter se*. *Lopes v. Reederei Richard Schroder*, 225 F. Supp. 292, 297 (E.D. Pa. 1963).

Indeed, the courts have consistently held Section 1350 to be applicable only to actions which involve the standards of conduct "which nations have established to control their relationships with one another." *Valanga v. Metropolitan Life Insurance Co.*, 259 F. Supp. 324, 328 (E.D. Pa. 1966); see *Damaskinos v. Societa Navigacion Interamericana, S.A.*, Pan., 255 F. Supp. 919 (S.D.N.Y. 1966).

Since plaintiffs have alleged neither a violation of the law of nations, nor that the conduct of which they complain violated a treaty of the United States, there can be no Section 1350 jurisdiction over this action.

Section 302 of the New York Civil Practice Law and Rules

Section 302 of the CPLR provides that certain acts by non-domiciliaries, either within the State of New York or without the State of New York which have an effect within it, may give rise to personal jurisdiction. As defendants Murphy, Taylor and Havens Wandless have not raised the issue of personal jurisdiction, an application of the provisions of CPLR 302 to their conduct is irrelevant to the questions at bar.

Moreover, it is clear that a personal jurisdiction statute such as CPLR 302 is procedural rather than substantive and does not extend the power of a Federal court beyond its normal subject matter jurisdiction. *Cf. Gardner v. United States*, 246 F. Supp. 1014, 1015 (S.D.N.Y. 1965).

Pendent Jurisdiction

In order to promote the interests of judicial economy, convenience and fairness to litigants, the Federal courts may exercise "pendent" jurisdiction over state law claims

when there are Federal claims before the court and the relationship between the state and Federal claims is such that together they constitute but one case. *United Mine Workers of America v. Gibbs*, 383 U.S. 715, 725 (1966). However, pendent jurisdiction is not a "free pass" into the Federal courts for plaintiffs asserting essentially state claims.

It is settled law that the district courts may not exercise pendent jurisdiction over state claims if subject matter jurisdiction over the accompanying Federal claims is lacking. When Federal claims are dismissed before trial, state claims with no independent basis of Federal jurisdiction must also be dismissed. *United Mine Workers of America v. Gibbs*, *supra* at 726; *Kavit v. A.L. Stamm & Co.*, 491 F.2d 1176, 1179 (2d Cir. 1974). Thus, as plaintiffs' only Federal claims are based on the securities laws, and it has already been demonstrated that there is no basis for exercising jurisdiction over those claims, plaintiffs' pendent claims must also fall.

CONCLUSION

The decision of the district court should be reversed, and this Court should enter an order directing the district court to dismiss the complaint herein for lack of subject matter jurisdiction.

Respectfully submitted,

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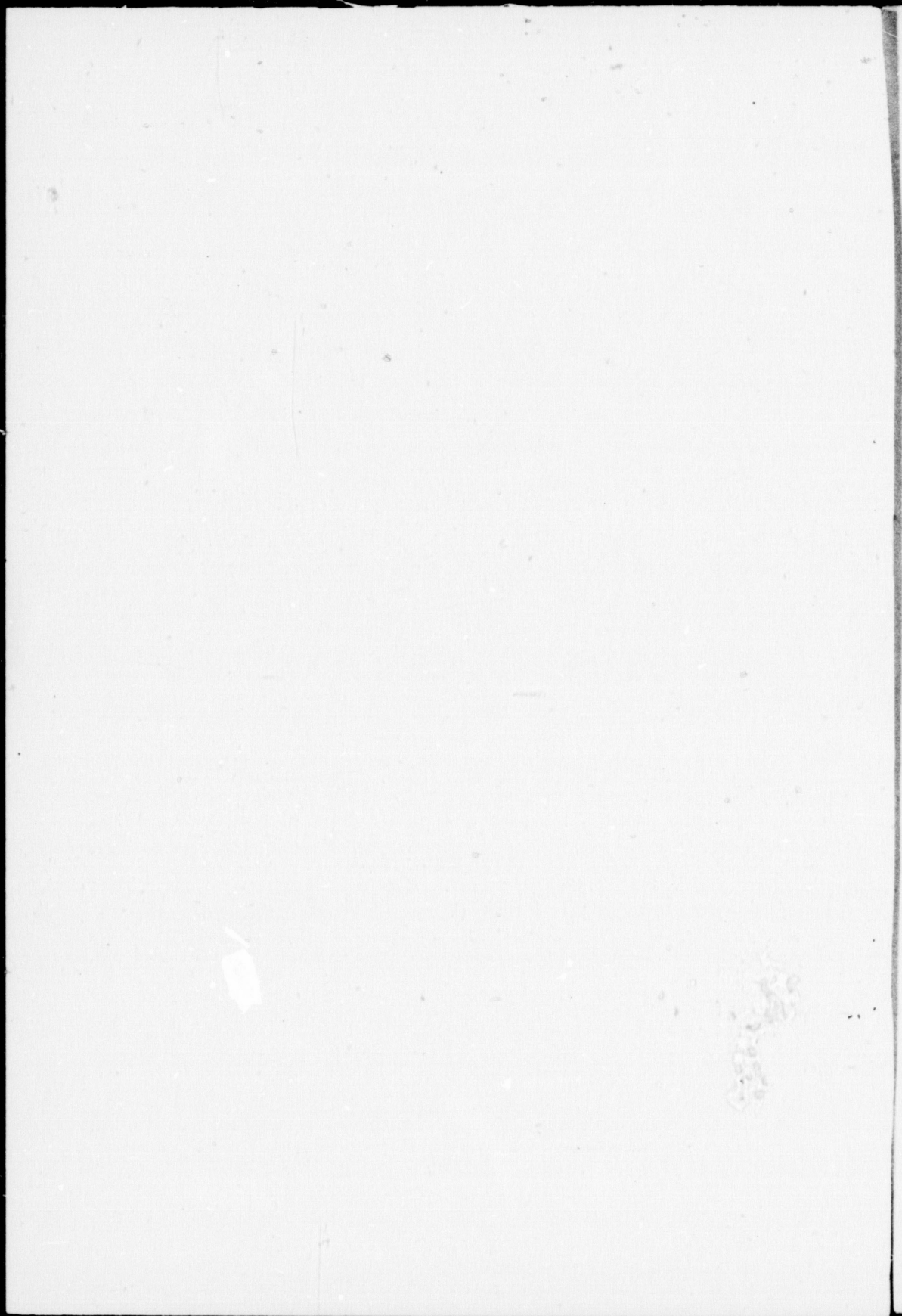
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Service of 2 copies of this within

Brief is admitted this

13 day of January 1975

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